ST 00-0031-PLR 11/30/2000 COMPUTER SOFTWARE

If transactions for the licensing of computer software meet all of the criteria provided in part (1) of subsection (a) of Section 130.1935, the transfer of the software will not be subject to Retailers' Occupation Tax liability. See 86 Ill. Adm. Code 130.1935. (This is a PLR.)

November 30, 2000

Dear Xxxxx:

This Private Letter Ruling, issued pursuant to 2 Ill. Adm. Code 1200 (which can be found at http://www.revenue.state.il.us/legalinformation/regs/part1200), is in response to your letter of October 4, 2000. Review of your request for a Private Letter Ruling disclosed that all information described in paragraphs 1 through 8 of subsection (b) of the enclosed copy of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to COMPANY for the issue or issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that neither COMPANY nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

In your letter, you have stated and made inquiry as follows:

Please treat this letter as a private letter ruling request for the Illinois Department of Revenue ('Department') to issue a formal opinion concerning the taxability under the Illinois Retailer's Occupation Tax and Use Tax of COMPANY licenses of computer software to its various customers. This request is made under Department Regulation Section 1200.110. COMPANY is not currently under audit or investigation concerning the matters for which this opinion request is being made. Enclosed is a power of attorney authorizing my representation of COMPANY.

To the best of COMPANY and this writer's knowledge, the Department has not previously ruled on the same or a similar issue for COMPANY or a predecessor, and neither COMPANY nor any of its representatives have previously submitted the same or a similar issue to the Department, but withdraw it before a letter ruling was issued.

Relevant Facts

COMPANY is in the business of selling both computer hardware and computer software to its business customers throughout the United States. In this regard, it purchases this computer hardware and computer software from various manufacturers and suppliers. The computer software it purchases is subject to a license agreement from the software manufacturer or supplier.

When COMPANY sells computer hardware with accompanying computer software, it enters into a Master License Agreement with its business customers, a copy of which is attached to this private letter ruling request. This license agreement incorporates by reference the terms of the manufacturer or supplier's license agreement, and supplements those terms with the terms of the COMPANY Master License Agreement.

As can be seen from the attachment, COMPANY's Master Lease Agreement contains the five requirements of Department Regulation Section 130.1935(a). A representative Master License Agreement is attached.

COMPANY's Master License Agreement is in writing and signed by both COMPANY and its business customer. The Agreement restricts the customer's duplication of the software and restricts the use of the software without express written approval of COMPANY, when such use exceeds the manufacturer's underlying software license. The License Agreement also prohibits the customer's license, relicense, sublicense, or transfer of the software to any third party (except a related party). COMPANY's License Agreement allows the customer to obtain another copy of the software at minimal or no cost to the customer, if the software is lost or damaged by the customer. Lastly, at the end of the license period, the business customer must destroy or return all copies of the software to COMPANY. Therefore, since COMPANY's Master License Agreement meets all five requirements of the Department's Regulations, it qualifies as a non-taxable license. Consequently, COMPANY's transfer/sale of software subject to this Master License Agreement would not be a 'taxable retail sale' under the Illinois Retailer's Occupation Tax or Service Occupation Tax.

Opinion Requested

1. COMPANY's purchases of computer software from software manufacturers and suppliers for resale to its business customers, subject to COMPANY's Master License Agreement, qualifies as purchases for resale not taxable under the Illinois Retailer's Occupation Tax and Use Tax.

2. COMPANY's sale of computer software under its Master License Agreement is exempt from Illinois Retailer's Occupation Tax and Use Tax as not being a 'taxable retail sale.'

Relevant Law And Analysis

Under both the Illinois Retailer's Occupation Tax and Use Tax, a purchase of computer software for purposes of 'resale' is not subject to tax. 35 ILCS 120/1; 35 ILCS 105/2. Therefore, COMPANY's purchases of computer software for resale to its business customers subject to its Master License Agreement would be purchases for resale not subject to Illinois Retailer's Occupation Tax and Use Tax. This conclusion is consistent with Regulation Section 130.1935 which states that any transfer of canned software is a sale subject to the Retailer's Occupation Tax and Use Tax. Consequently, COMPANY's purchase of the software for purposes of resale to its customers would qualify as an exempt purchase for resale under the Retailer's Occupation Tax and Use Tax.

Moreover, the fact that COMPANY's ultimate resale of the software qualifies as an exempt license under Regulation Section 130.1935, does not change the fact that COMPANY's purchase of the software was still a purchase for resale. Section 130.1935 merely recognizes that a subsequent sale is a non-taxable retail sale if it is subject to the five license requirements of Section 130.1935(a)(1). This is also consistent with the example provided in Regulation Section 130.1935(c)(2), which reiterates that canned software can be purchased for 'resale' by a computer programmer, even when the programmer thereafter modifies the software and sells it as ''tax exempt' modified

software (*i.e.*, custom computer software) to its customer. Here again, it is emphasized that the initial purchase is still for resale, even though the ultimate sale of the software may be exempt from tax.

Finally, as previously mentioned, Department Regulation 130.1935 provides that sales of computer software which meet the five requirements of a non-taxable license will not be deemed a 'taxable retail sale' under Illinois Retailer's Occupation Tax and Use Tax. COMPANY's Master License Agreement contains all five requirements of Regulation Section 130.1935. See also ST 99-0004 – PLR. Therefore, COMPANY's transfer of its computer software to its business customers subject to its Master License Agreement would not be a taxable retail sale under the Illinois Retailer's Occupation Tax and Use Tax.

Conclusion

We believe, based upon the wording of the Master License Agreement and the applicable Regulations of the Department (specifically, Section 130.1935), that COMPANY can purchase computer software for resale from its manufacturers and suppliers by providing a resale certificate to such manufacturers and suppliers stating that COMPANY will be reselling that software to its customers in Illinois. Moreover, because COMPANY's ultimate sale of such software is subject to a Master License Agreement which qualifies under the five requirements of Regulation Section 130.1935(a), the retransfer of such computer software would not be deemed a 'taxable retail sale' under Illinois law. Therefore, there would be no Illinois Retailer's Occupation Tax and Use Tax due on such transfers.

Neither COMPANY nor the undersigned has knowledge of any other regulation or ruling by the Department which contradicts the above analysis. If the Department needs more information or is considering not providing the opinions requested above, COMPANY requests that there be a conference between its representative and the Department before any Private Letter Ruling is issued.

Thank you again for your time and cooperation in this matter.

If transactions for the licensing of computer software meet all of the criteria provided in part (1) of subsection (a) of Section 130.1935, the transfer of the software will not be subject to Retailers' Occupation Tax liability. See the enclosed copy of 86 Ill. Adm. Code 130.1935. A license of software is not a taxable retail sale if:

A) it is evidenced by a written agreement signed by the licensor and the customer;

B) it restricts the customer's duplication and use of the software;

C) it prohibits the customer from licensing, sublicensing or transferring the software to a third party (except to a related party);

D) the licensor has a policy of providing another copy at minimal or no charge if the customer loses or damages the software, or of permitting the licensee to make and keep an archival copy, and such policy is either stated in the license agreement, supported by the licensor's books and records, or supported by a notarized statement made under penalties of perjury

by the licensor; and the vendor will provide another copy at minimal or no charge if the customer loses or damages the software; and

E) the customer must destroy or return all copies of the software to the vendor at the end of the license period. This provision is deemed to be met, in the case of a perpetual license, without being set forth in the license agreement.

Based upon our review of the COMPANY Master License Agreement enclosed with your letter ruling request, the transfer or sale of computer software subject to that Master License Agreement would meet the requirements of part (1) of subsection (a) of Section 130.1935 of the Department's Administrative rules and would not be a taxable retail sale under the Illinois Retailers' Occupation Tax Act (35 ILCS 120/1 et seq.) and Use Tax Act (35 ILCS 105/1 et seq.). COMPANY may purchase canned computer software for resale that is being transferred subject to COMPANY Master License Agreement.

The facts upon which this ruling are based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

I hope this information is helpful. If you have questions regarding this Private Letter Ruling you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at www.revenue.state.il.us or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Terry D. Charlton
Associate Counsel

TDC:msk
Enc.